PUBLIC BANK BHD.

v.

METRO CONSTRUCTION SDN. BHD.

HIGH COURT MALAYA, KUALA LUMPUR
LIM BENG CHOON J
[ORIGINATING SUMMONS NO. 31-699-86]
13 FEBRUARY 1990

COMPANY LAW: *Third party charges created by directors - Ultra vires memorandum and articles of association - Procedural or substantive ultra vires - Nature and effect of memorandum and articles - Construction of object clauses - Main or principal objects of a company - Whether party bound to inquire into company's capacity - Good faith - Valid resolutions - Whether binding on company - Benefit of third party - Actual apparent or ostensible authority - Companies Act 1965, s. 20(1).*

The defendants M, who were the registered owners of the said land executed two third party charges in favour of the plaintiff, PBB, to secure repayment of two loans amounting to RM1.2 million given by PBB to T. Form 16A and the annexures were signed by two persons who claimed to be directors of M; these documents were duly affixed with the company seal - the charge was registered.

T failed to repay the loans and PBB issued a Form 16D notice M which M did not comply with. PBB then applied for an order of sale by public auction. L, a director and major shareholder of M, apposed the action, claimed that he and five others directors had been tricked into resigning and that Y1 and Y2 were appointed directors - a company resolution dated 4 January 1984 to this effect was passed. L alleged that after obtaining the original title deed of the land, Y1 and Y2 fraudulently passed another resolution dated 21 November 1984, authorising M to create the two-third party charges. Further, L submitted than M had no dealing whatsoever with T, that Y1 and Y2 failed to pay for the shares of the company.

On 12 February 1988 PBB's application was granted and the auction was fixed on 19 August 1988; On 15 September 1988 M applied *ex parte* for an order that PBB be stayed from execution of the order of 12 February 1988 and also sought leave to set aside this order.

G, another director of M contended that the charges were null and void as the resolution authorising the two charges did not comply with M's articles of association that is, for creation of a charge over M's property for the benefit of a third party, the consent and resolution of the general meeting was required. M's *ex parte* application was allowed on 16 September 1988. PBB applied to set aside the order granting the stay whereby the manager of PBB, asserted that PBB had no knowledge of the purported frauds by Y1 and Y2, based on the resolution dated 21 November 1984, the charges were valid and enforceable and that PBB was not obliged to inquire into M's power to grant third party charges. G also said that the six shareholders of M had not acted *bona fide* in their application to set aside the order for sale.

M raised two issues:

(a) whether the third party charges were *ultra vires* M's memorandum of association (substantive *ultra vires)* and if so, whether the transactions are saved by s. 20(1), Companies Act 1965.

(b) notwithstanding the fact that if the charges were *intra vires*, the memorandum, whether the charges bound the company if they were created by the directors acting *ultra vires* the articles of association (procedural *ultra vires*); further whether s. 20 of the Act was then applicable;

Held:

[1] Although a company's memorandum must state the objects of the company, it is not uncommon that a memorandum does usually set out as objects of the company many of the powers which the company would be entitled to exercise in carrying out its objects. Such a practice, though criticised in *Broughman's* case does not render the memorandum inconclusive.

[2] (a) An attempted departure from the objects stated in the memorandum is as invalid as if the memorandum were a statute of incorporation; it is *ultra vires* the company and cannot be validated by assent of a general meeting of the members or by taking judgment against the company by consent or by estoppel.

(b) in the construction of the object clauses of a memorandum, the ordinary rules applicable to the construction of documents apply equally well to the construction of the object clauses.

(c) if a transaction is covered by the object clauses, a party to the transaction is not bound to inquire as to the company's capacity to enter into to it or as to any such limitation on the director's powers and the party will be presumed to have acted in food faith unless the contrary is proved

[3] On the facts of this case:

(a) object under Clause 3(31) is wide enough to indicate that one of the objects of M is to carry on the business akin to that of a financial institution which includes that of raising money from loan by way of a charge on real properties.

(b) In carrying out this kind of business, M is empowered under Clause 3(44) to borrow money;

(c) M is also empowered under Clause 3(50) to guarantee or give securities for any payment of money, repayment of loan or any credit facilities including credit facilities given by banks in the manner as provided therein.

(d) as a result, the creation of the two third party charges is within M's power.

[4] (a) As the two charges were executed on 13 December 1984 and the action for order for sale of land was instituted on 20 March 1986, one cannot impute knowledge of the fraud committed by Y1 and Y2 to PBB.

(b) the allegations of M relate to Y1 and Y2 acting fraudulently in excess of their authority; however the fraud committed by Y1 & Y2 against the shareholders and the excess of authority on the part of Y1 & Y2 is a matter only between the Y1 & Y2 and the shareholders;

(c) there is nothing improper or illegal in the transactions which led to the creation of the charges; therefore the bank executed the two charges in good faith and in pursuance of transactions which *prima facie* are lawful and properly carried out.

[5] As to the whether the directors could borrow money for the benefit of a third party:

(a) under Article 86, Y1 and Y2 could exercise the powers of the company pursuant to Articles 102 & 103; therefore the resolution of the company dated 21 November 1984 which was proposed and adopted by Y1 and Y2 were validly made pursuant to Articles 119 and 124;

(b) therefore, Y1 and Y2 had actual authority to execute the two charges with PBB;

(d) even assuming the 'actual' authority is found wanting, it cannot be said that Y1 & Y2 did not have, at the material time, an "apparent" or "ostensible" authority to exercise the charges.

[6] Section 20(1) of the Act abolishes the otherwise rigorous effect of the *ultra vires* doctrine; even if the third party charges were *ultra vires* the company's memorandum and articles of association, this could be saved by s. 20(1) of the Act.

[PBB's application to revoke order of 16 September 1988 allowed M's plea for leave to set aside order of 12 February 1988 revoked.]

Cases referred to:
Anglo Overseas Agencies Ltd. v. Green [1960] 3 All ER 244
Charterbridge Corporation Ltd. v. Lloyds Bank Ltd. [1970] Ch 62
Cotman v. Broughman [1918] AC 514
Freeman v. Buckhurst Park Properties [1964] 1 All ER 630
Great North-West Central Railway v. Charlebois [1899] AC 114
In re David Payne & Co. Ltd. [1904] 2 Ch 608
Re Introduction's [1969] 1 All ER 887
Rolled Steel Ltd. v. British Steel Corporation [1986] 1 Ch 246
The Royal British Bank v. Turquand Vol. 119 ER KB 474

Legislation referred to:
Companies Act 1965, s. 20(1)
National Land Code 1965, ss. 242, 254

Other sources referred to:
Sourcebook of Singapore and Malaysian Company Law, by Philip N. Pillai 1975 Edn. at p. 121

For the plaintiff - C.K. Yeoh; M/s. Chooi & Company
For the defendant - V.L. Yiew; M/s. Ngeow & Maurice Gomes

JUDGMENT

Lim Beng Choon J:

Metro Construction Sdn. Bhd. (Metro) the defendants in this originating summons, are the registered owners of the land held under Grant 1st Grade Lot 297 section 1, Tanjung Tokong, Penang (the land). They executed two third party charges on the land in favour of Public Bank Bhd. (the bank) to secure the repayments of the two loans amounting to RM1.2 million given by the bank to the third party, Tenaga Muhibbah Sdn. Bhd. (Tenaga). The two charges were duly registered under s. 242 of the National Land Code 1965 on the same date, that is, on 13 December 1984. The instruments effecting the charges namely forms 16A with the annexures, were signed by two persons who claimed to be directors of Metro and the said instruments were duly affixed with the company's seal. Apparently Tenaga failed to repay the loans and the accrued interests and on 24 December 1985, the bank accordingly issued a notice in form 16D pursuant to s. 254 of the National Land Code to Metro demanding

payment of the outstanding sum within the period as specified in the notice failing which the bank would apply to the Court for an order for the sale of the land. Metro had failed to settle the outstanding sum within the specified period and the bank accordingly instituted this action on 20 March 1986 for an order for the sale of the land by public auction to satisfy the outstanding sum owed to them by Tenaga. An affidavit was simultaneously filed by the bank stating the grounds in support of the application for an order for sale of the land (encl. 2).

After the service of this originating summons on Metro was effected, one Lee Khai Hong, who claimed to be one of the directors and the major shareholder of Metro, filed in an affidavit affirmed on 16 September 1987 (encl. 8) to oppose the proceeding to sell the land. In his affidavit he alleged that some time in January 1984 one Yeoh Kok Ooi and one Yeoh Seng Lye (for convenience I shall refer them as the two Yeohs unless otherwise specifically stated), on the pretext of acquiring Metro by the purchase of all the shares of Metro, tricked him and the other five directors to resign and to appoint the two Yeohs to be directors in place of them. He produced a copy of the company's resolutions dated 4 January 1984 which was annexed to his affidavit as Exh. 'A2'. The resolutions proposed and accepted by all the directors can be summarised thus:

(a) the resignation of all the six directors was to be of immediate effect.

(b) the approval of the transfer of the 400,000 ordinary shares from the six current shareholders to the two Yeohs at the purchase price specified in the resolution was accepted.

(c) step would be taken to effect the transfer by the cancellation of the old share certificates and the issue of new certificates.

(d) the two Yeohs were duly appointed as directors of the company with immediate effect.

(e) Yeoh Seng Lye was made the chairman of the company with immediate effect.

(f) Yeoh Kok Ooi was appointed as managing director of the company with immediate effect.

It was also alleged that after the resolutions were passed and adopted the two Yeohs persuaded the former directors to surrender the original title deed of the land to the two Yeohs which they did. Thereupon on 21 November 1984 the two Yeohs without the knowledge, authority or approval of the company secretary or any of the shareholders unilaterally passed a resolution authorising the company to create the two third party charges on the land. A copy of the said resolution dated 21 November 1984 was annexed to the affidavit as Exh. 'A5'. The resolution was conveyed in a note bearing the company's name and address and it said:

> Pursuant to the authority given by Article 124 of the company's articles of association, we, the undersigned, being all the directors of the abovenamed company hereby resolved:
>
> That the company do and is hereby authorised to create a third party first and second legal charge on the property of the company known as Lot 297, section 1, Bandar Tanjong Tokong, Daerah Timur Laut, Pulau Pinang for banking facilities granted to M/s. Tenaga Muhibbah Sdn. Bhd. by M/s. Public Bank Berhad in the total amount of RM1,200,000 (One Million and Two Hundred Thousand Only) and that Mr. Yeoh Kok Ooi @ Yeoh Kok Wooi be and is hereby authorised to execute the charge and other documents pertaining to the above facilities, and the company be and is hereby also authorised to execute a corporate guarantee for the same banking facilities and the common seal of the company be affixed to the relevant documents in the above connection.

It was dated 21 November 1984 and was signed by Yeoh Seng Lye and Yeoh Kok Ooi. The deponent went on to say that it was only some time in 1986 that the former directors of Metro were made aware of the two third party charges created by the two Yeohs with the bank. He asserted that Metro had no dealing whatsoever with Tenaga, neither did Metro receive any moneys from the bank in respect of the charges. It also appeared that the two Yeohs had failed to pay for the shares of the company. The shares still remain with the six shareholders of which Lee Khai Hong holds the majority shares.

At the hearing of this originating summons, an order in terms of the summons was made by Dato' Ajaib Singh J (as he then was) on 12 February 1988 and the date of the auction of the land was fixed on 19 August 1988. Summons-for-Directions was duly taken out on 14 April 1988 and on 22 June 1988 the Senior Assistant Registrar of this Court made an order regarding the procedure of the sale. The reserved price of the land was fixed at RM910,000.

On 15 September 1988, Metro filed in an *ex parte* summons-in-chambers (encl. 13) to request the Court for an order that the plaintiff be stayed from the execution of the order of the Court dated 12 February 1988 directing the sale of the land by public auction. They also requested that Metro be granted leave to set aside the said order. Apparently the auction of the land had not yet been carried out although it is not clear as to why it was not done. In support of the application, an affidavit (encl. 12) was filed by one Goh Nai Kooi on 15 September 1988 in his capacity (so he claimed) as a director of Metro. He repeated the allegations as set out in the earlier affidavit of Lee Khai Hong and further stated that the two third party charges were null and void as the resolution authorising the two charges was not made in compliance with the company's memorandum and articles of association. It went on to say that under the articles of association of the company the directors of the company were empowered only to borrow or raise money or secure repayment or payment of such sums by mortgage or charge upon any of the properties of Metro for the purposes of the company. To enable a charge over Metro's property created for the purpose or benefit of a third party the consent and resolution of the general meeting was required. In creating the said charges the two Yeohs had failed to comply with these pre-requisites. It was also alleged that the solicitors acting for the bank had been informed by letter dated 24 June 1987 written by Metro's solicitors that police investigation had commenced against the two Yeohs.

The *ex parte* application of Metro came on for hearing on 16 September 1988 and Datuk Abdul Razak J allowed the application and made an order in terms of the application.

The bank thereafter applied to set aside the order granting the stay. Their application by way of summons-in-chambers was filed on 28 October 1988. In support of the application, the manager of the bank, Toh Wah San filed in an affidavit (encl. 19). The contents of this affidavit may be briefly summarised as follows:

(a) the bank had no knowledge whatsoever of the purported frauds committed by the two Yeohs when the third party charges were executed.

(b) the resolution dated 21 November 1984 authorising the creation of the two charges was made available to the bank by Metro when the said charges were executed. The said charges were therefore valid and enforceable by the bank upon default by Tenaga.

(c) the bank was not obliged to enquire into the power of Metro to grant third party charges. A copy of Form 49 conveying the appointment of the two Yeohs as directors to the Registrar of Companies was produced and annexed to the affidavit.

It was further asserted by Toh that upon receipt of this originating summons by Metro's former solicitors, Metro attempted to negotiate with the bank's solicitors for a settlement of the outstanding sum. As late as 9 February 1987 all the shareholders of Metro, through their former solicitors had indicated that they were making arrangements to salvage the company and redeem the land and that they would be coming up with some concrete proposals for settlement. The notice of appointment to hear this originating summons was served on Metro on 26 June 1987. But none of the representatives or shareholders of Metro nor their solicitors thought it fit to appear at the hearing on the originating summons when the order for sale of the land was made on 12 February 1988. Likewise metro's representatives, shareholders and solicitors had also failed to appear at the hearing of the summons-for-direction made by the SAR though Metro was duly served with the summons. The bank also produced a letter dated 27 September 1986 annexed as exhibit 'PBB5' to Toh's affidavit. The letter was written by the solicitors acting for the shareholders of Metro and addressed to the two Yeohs. It indicated *inter alia* that unless the two Yeohs took steps to redeem the land and make good the losses sustained by the shareholders, appropriate civil and criminal proceedings would be initiated by the shareholders. It also said that the shareholders were not prepared to accept Yeoh Seng Lye's offer to resign as director of Metro made on 8 August 1985. By reason of the conduct of six shareholders of Metro it was therefore alleged that they had not acted *bona fide* in their application to set aside the order for sale.

Counsel for Metro in his written submissions tendered at the hearing of the bank's application to set aside the order to stay the execution of the sale of the land has posed two questions to this Court:

(i) Whether the third party charges were *ultra vires* the company's memorandum of association (substantive *ultra vires* and if so whether the transactions are saved by s. 20(1) of the Companies Act 1965).

(ii) Whether the third party charges even if *intra vires* the company's memorandum, if created by the directors acting outside and beyond their powers as provided in the company's articles of association (procedural *ultra vires*) binds the company and whether s. 20 Companies Act 1965 applies to such circumstances.

To answer these two questions, it is necessary to set out the relevant clauses and articles of the memorandum and articles of association of Metro which have been produced and annexed as Exh. 'GNK2' to the affidavit of Goh Wai Kooi in encl. 12 of the Court's file. In extracting the relevant clauses from the memorandum of association I must bear in mind that although a company memorandum must state the objects of the company, it is not uncommon that a memorandum does usually set out as objects of the company many of the powers which the company would be entitled to exercise in carrying out its objects. Such a practice, though criticised in *Cotman v. Broughman* [1918] AC 514 at 522, 523 does not render the memorandum inconclusive. A cursory glance at the memorandum of Metro will show that the company was established to carry on a very wide range of business enterprises such as housing development, importing, exporting, manufacturing and sales of many kinds of goods, running of hotels and restaurants, operating travel agencies, mining and quarries. One significant object is set out in subclause (31) of Clause 3 which reads:

> To carry on business as financiers, factors, moneylenders, hire-purchase financiers, concessionaires, manufacturers representatives, forwarding and collecting agents, insurance agents, real property and estate brokers and agents, commission, managing and general agents, indenting agents, franchise holders and dealers in options of all kinds and to promote, undertake, execute,

operate, transact, supervise or otherwise carry on all kinds of financial, trading, manufacturing, processing, milling, curing, packing and maintenance servicing business or other kinds of business which may be capable of being carried on in connection therewith.

The powers to carry this object are expressed in the following subclauses of the said clause 3 of the memorandum:

(40) To invest, lend, advance or otherwise deal with the company's moneys not immediately required in such a manner as shall from time to time be determined and to draw, accept, endorse, discount, issue or otherwise execute debentures, mortgages, bills of lading or exchange, promissory notes, guarantees and other negotiable or transferable instruments.

(41) To lend and advance money on any term as may be determined to customers, agents, dealers or employees of the company or other corporations or persons who have dealings with the company and to guarantee the payment of any loan made to any of them.

(44) To borrow, raise or otherwise secure the payment of money or loans by mortgage, guarantee, issue of debentures or in other manner which may be beneficial to the company and for the purposes or for any lawful purposes to charge all or any of the properties, assets or uncalled capital, present and future, and collaterally or further to secure any securities of the company by a trust deed or other assurance.

(50) To guarantee or become liable to or give securities for any payment of money, repayment of loans or any credit facility, performance of contracts or duties or any issue of letters of guarantees, hypothecation or credit by any bank, company, person or others on account or instruction of the company.

The relevant articles of the articles of association of Metro which are useful to set out in full are:

4. Any branch or kind of business which by the memorandum of association of the company or by these articles is either expressly or by implication authorised to be undertaken by the company, may be undertaken by the directors at such time or times as they shall think it fit and further may be suffered by them to be in abeyance, whether such a branch or kind of business may have been actually commenced or not, so long as the directors may deem it expedient not to commence or proceed with such a branch or kind of business.

86. Unless otherwise determined by a general meeting, the number of directors shall not be less than two nor more than seven.

98. The directors may entrust to and confer upon the managing director, joint managing directors and assistant managing directors any of the powers exercisable by them as directors on such terms and conditions and with such restrictions as they think fit and either collaterally with or to the exclusion of their own powers and may from time to time revoke, withdraw, alter or vary all or any of the powers entrusted or conferred.

102. The business of the company shall be managed by the directors, who may pay all expenses of and preliminary and incidental to promotion, formation, establishment and registration of the company as they think fit, and may exercise all such powers of the company and do on behalf of the company all such acts as may be exercised and done by the company except such powers or acts which by the Act or by these articles are required to be exercised or done by the company in general meeting, subject nevertheless to the provisions of these articles, to the provisions of the Act and to such regulations being not inconsistent with the aforesaid regulations or provisions as may be prescribed by the company in general meeting, but no regulation made by the company in general meeting shall invalidate any prior act of the directors which would have been valid if such regulations had not been made.

103. The directors shall have power to borrow or raise money from tim*e* **to time for the purpose of the company or secure the payment of such a sum as they think fit and may secure the repayment or payment of such sums by mortgage or charge upon all or any of the properties or assets of the company** or by the issue of debentures (whether at par or at a discount or premium) or otherwise as they may think fit. (Emphasis is mine).

119. The quorum necessary for the transactions of the business may be fixed by the directors and unless so fixed at any other number, shall be two. A meeting of the directors at which a quorum is present shall be competent to exercise all the powers and discretions for the time exercisable by the directors.

124. A resolution in writing signed by all the directors shall be as valid and effectual for all purposes as a resolution passed at a meeting of the directors duly convened, held and constituted.

126. The seal shall not be affixed to any instrument except by the authority of a resolution of the board of directors and in the presence of any two directors or of at least one director and of the secretary or such other person as the directors may appoint aforesaid shall sign every instrument to which the seal is so affixed in their presence and in favour of any person *bona fide* dealing with the company. Such signatures shall be conclusive evidence of the fact that the seal has been properly affixed.

In my consideration of the first limb of question (i) posed by Counsel for Metro namely whether the third party charges are *ultra vires* the company's memorandum of association, it must be noted that a company's objects as stated in its memorandum cannot be departed from. An attempted departure is as invalid as if the memorandum were a statute of incorporation; it is *ultra vires* the company and cannot be validated by assent of a general meeting of the members or by taking judgment against the company by consent or by estoppel. This proposition is neatly stated in the following short passage of the judgment of the Privy Council in *Great North-West Central Railway v. Charlebois* [1899] AC 114 at 124.

> It is quite clear that a company cannot do what is beyond its legal powers by simply going into Court and consenting to a decree which orders that the thing shall be done.

Next it must be borne in mind that in the construction of the object clauses of a memorandum, the ordinary rules applicable to the construing of documents apply equally well to the construction of the object clauses. There is no special rule of interpretation by reference to what are supposed to be the main or principal objects of a company where the question is whether something done or proposed to be done is *ultra vires.* Thus in *Cotman v. Broughman* [1918] AC 514, Lord Parker said at pp. 520 - 521:

> The questions whether or not a transaction is *ultra vires* is a question of law between the company and a third party. The truth is that the statement of a company's object in its memorandum is intended to serve a double purpose. In the first place it gives protection to subscribers, who learn from it the purposes to which their money can be applied. In the second place it gives protection to persons who deal with the company, and who can infer from it the extent of the company's powers. The narrower the objects expressed in the memorandum the less is the subscribers' risk, but the wider such objects the greater is the security of those who transact business with the company. Moreover, experience soon showed that persons who transact business with companies do not like having to depend on inference when the validity of a proposed transaction is in question. Even a power to borrow money could not always be safely inferred, much less such a power as that of underwriting shares in another company. Thus arose the practice of specifying powers as objects, a practice rendered possible by the fact that there is no statutory limit on the number of objects which may be read as ancillary to and exercisable only for the purpose of attaining what might be held to be

> the company's main or paramount object, and on this construction no one could be quite certain whether the Court would not hold any proposed transaction to be *ultra vires*. At any rate, all the surrounding circumstances would require investigation. Fresh clauses were framed to meet this difficulty, and the result is the modern memorandum of association with its multifarious list of objects and powers specified as objects and its clauses designed to prevent any specified object being read as ancillary to some other object.

The proposition is reiterated by Salmond J in *Anglo Overseas Agencies Ltd. v. Green* [1960] 3 All ER 244. The third general principle which is worthy of notice is that if a transaction is covered by the object clauses, a party to the transaction is not bound to inquire as to the company's capacity to enter into it or as to any such limitation on the directors' powers and the party will be presumed to have acted in good faith unless the contrary is proved. In the *Broughman's* case Lord Parker reiterated this principle at p. 521 of the reported case:

> A person who deals with a company is entitled to assume that a company can do everything which it is expressly authorised to do by its memorandum of association, and need not investigate the equities between the company and its shareholders.

This passage in the judgment of Lord Parker was followed by Harman LJ in *Re Introductions's* [1969] 1 All ER 887 at 890 who went on to cite the following words appearing in the headnote of the case of *Re David Payne & Co. Ltd.*:

> Where a company has a general power to borrow money for the purposes of its business, a lender is not bound to enquire into the purpose for which the money is intended to be applied, and the misapplication of the money by the company does not avoid the loan in the absence of knowledge on the part of the lender that the money was intended to be misapplied.

Reverting to the object clauses of the memorandum of association of Metro, I have no doubt that the object under Clause 3 subclause (31) is wide enough to indicate that one of the objects of Metro is to carry on the business akin to that of a financial institution which needless to say includes that of raising money from loan by way of a charge on real properties. The phrases "To carry on business as financiers", "to promote undertake, execute, operate, transact, supervise or otherwise carry on all kinds of financial trading" and "or other kinds of business which may be capable of being carried on in connection therewith" clearly support this proposition. In carrying out this kind of business, Metro is empowered under subclause (44) of Clause 3 to borrow money as provided in that subclause. Likewise Metro is also empowered under subclause 50 of the said Clause 3 to guarantee or give securities for any payment of money, repayment of loan or any credit facilities including credit facilities given by banks in the manner as provided therein. In the circumstances, it cannot be gainsaid that the creation of the two third party charges are within the object clauses of Metro. It cannot likewise be disputed that Metro has the necessary powers to create these two third party charges. But it was then contended firstly that as the two charges were created not for the benefit of the company but for the benefit of third party, the creation of the two charges was therefore outside the borrowing power conferred under subclause (44). Secondly it was said that as the said charges were created "not on account or instruction of the company" the creation likewise was in breach of subclause (50). As the first contention is inter-related to the question (ii) posed by the Counsel for Metro, I will deal with this contention in my answer to the said question (ii) later in this judgment. In considering the second contention, it is to be noted that there is no plea that the bank had at the material time knowledge of the fraud committed by the two Yeohs against the shareholders of Metro. Neither is there any statement setting out facts from which such knowledge can be inferred. The only allegations made against the bank were that a police report had been lodged on 4 April 1987 against the two Yeohs and that the bank's solicitors were informed on 24 June

1987 of the said report and the commencement of the investigation by the police on that report. Bearing in mind that the two charges were executed on 13 December 1984 and this action for an order for the sale of the land was instituted on 20 March 1986, how can one impute knowledge of the fraud committed by the two Yeohs to the bank? So the allegations of Metro amount to no more than that as between the two directors Yeoh Seng Lye and Yeoh Kok Ooi and the shareholders the said two directors had, in executing the two charges, acted fraudulently and in excess of their authority. But the fraud committed by the two directors against the shareholders and the excess of authority on the part of the said directors is a matter only between the said directors and the shareholders. More importantly when I look at the transactions leading to the creation of the two charges I cannot find anything improper or illegal in the transactions. From the return of the particulars of directors sent to the registrar of companies in Form 49 it was clearly stated that the two Yeohs were appointed directors of the company with effect from 4 January 1984 and that they were the only two directors; there were no other persons appointed as directors. The resolutions of the company dated 21 November 1984 authorising the creation of the two charges were said to have been made pursuant to Article 124 of the articles of association of Metro. The signatures of these two directors were affixed thereto. The instruments effecting the two charges were also signed by these two directors and the seal of the company was affixed to every one of the instruments. In the circumstances it cannot be disputed that the bank executed the two charges in good faith and in pursuance of transactions which *prima facie* are lawful and properly carried out. For these reasons and on the principles discussed above I have no hesitation in rejecting he contention of Counsel. If a further authority is required I would refer to the case of *The Royal British Bank v. Turquand* Vol. 119 English Reports Kings Bench 474 at 479 where it is said:

> Looking to the business to be carried on by this company, it might well be presumed that opening such an account and carrying on such dealings with a banking house as are described in the condition would be within the authority of the directors, and would be for the benefit of the shareholders. A mere excess of authority by the directors, we think, of itself would not amount to a defence. The bond being under the seal of the company, the gist of the defence must be illegality. If the directors had exceeded their authority to the prejudice of the shareholders by executing the bond, and this had been known to the obligees, illegality, we think, would have been shewn. The obligors in executing, and the obligees in accepting, the bond might be considered as combining together to injure the shareholders; the two parties would have been *in pari delicto*: and the action could not have been maintained. In such circumstances *potior est conditio defendentis*. But without the scienter, and without prejudice to the shareholders or any others whatsoever, illegality is not established against the obligees. If no illegality is shown as against the party with whom the directors contract under the seal of the company, excess of authority is a matter only between the directors and the shareholders.

I now turn to the first limb of question (ii) posed by Counsel namely that whether the third party charges if created by the directors acting outside and beyond their powers would bind the company. In his written submission the Counsel for Metro relied first on Article 102 of the articles of association of the company which empowered the directors of the company to manage the business of the company and to exercise all the powers and to act on behalf of the company subject nevertheless to the provisions of the articles of association. The second article relied on is Article 103 which says *inter alia* that "the directors shall have power to borrow or raise money from time to time for the purpose of the company." The Counsel contended that reading the two articles together the directors of Metro could only borrow money for the purpose of the company and not, as it happened here, for third party. Furthermore as the loans raised by the two charges were for the benefit of third party and not the company, subclause 44 of Clause 3 of the memorandum of association had also been

violated. In support of his contention Counsel drew my attention to a passage from the judgment of Diplock LJ in *Freeman v. Buckhurst Park Properties* [1964] 1 All ER 630 at 646 where the learned Judge after having analysed the relevant law, summarised the result of his analysis by stating four conditions which must be fulfilled to entitle a contractor to enforce against a company a contract entered into on behalf of the company by an agent who had no actual authority to do so. In fairness to the learned Counsel, he did not intend that I should read that passage in isolation and ignore what Lord Diplock had really said in his analysis of the law. I will therefore cite the following passage of the judgment where the learned Judge drew a distinction between an 'actual' authority of an agent and an 'apparent' or 'ostensible' authority:

> An "actual" authority is a legal relationship between principal and agent created by a consensual agreement to which they alone are parties. Its scope is to be ascertained by applying ordinary principles of construction of contracts, including any proper implications from the express words used, the usages of the trade, or the course of business between the parties. To this agreement the contractor is a stranger; he may be totally ignorant of the existence of any authority on the part of the agent. Nevertheless, if the agent does enter into a contract pursuant to the "actual" authority, it does create contractual rights and liabilities between the principal and the contractor.
>
> An "apparent" or "ostensible" authority, on the other hand, is a legal relationship between the principal and the contractor created by a representation, made by the principal to the contractor, intended to be and in fact acted on by the contractor, that the agent has authority to enter on behalf of the principal into a contract of a kind within the scope of the "apparent" authority, so as to render the principal liable to perform any obligations imposed on him by such contract. To the relationship so created the agent is a stranger. He need not be (although he generally is) aware of the existence of the representation. The representation, when acted on by the contractor by entering into a contract with the agent, operates as an estoppel, preventing the principal from asserting that he is not bound by the contract. It is irrelevant whether the agent had actual authority to enter into the contract. (*ibid* p. 644 D - G).

Now there is no dispute or at least it cannot be disputed that at the material time, Metro had only two directors namely Yeoh Kok Ooi and Yeoh Seng Lye, who were also the chairman and managing director respectively of the company. Under Article 86 it is provided that the number of directors shall not be less than two nor more than seven. It therefore follows that these two directors could exercise the powers of the company pursuant to Articles 102 and 103. Likewise the resolution of the company proposed and adopted by these two directors were validly made pursuant to Articles 119 and 124. Applying the principles laid down in *Freeman's* case *supra*, it cannot be disputed that the two directors had 'actual' authority to execute the two charges with the bank. Even assuming the 'actual' authority is found wanting (to which I cannot accede) it surely cannot be said that they did not have, at the material time, an "apparent" or "ostensible" authority to exercise the charges. But then it is said that the two directors could not borrow money if the borrowed money was not used for the purpose or benefit of the company. On the principle laid down in the *Broughman's* case and the *Re Introductions* Ltd's case cited earlier, I do not think such a contention can be sustained for that principle certifies that

> where a company has a general power to borrow money for the purposes of its business, a lender is not bound to enquire into the purpose for which the money is intended to be applied.

This principle is reiterated by Browne-Wilkinson LJ in *Rolled Steel Ltd. v. British Steel Corporation* [1986] 1 Ch 246 at pp. 305 - 306:

> In my judgment, the propositions in the last two paragraphs accord with the decisions *In Re David Payne & Co. Ltd.* [1904] 2 Ch 608 and *Charterbridge Corporation Ltd. v. Lloyds Bank Ltd.* [1970] Ch 62. As Slade LJ has pointed out, in the *David Payne* case the objects clause of the company stated expressly that the power to borrow was "for the purposes of the company's business," yet the borrowing (which was not in fact for the purpose of the company's business) was held not to be *ultra vires*. Buckley J, at p. 612, plainly treated the provision as a power, not an object. Vaughan Williams LJ held, at p. 615, that the fact that the validity of the debenture depended on whether or not the lender had knowledge of the impropriety, showed that the transaction was not *ultra vires*. Moreover, it was held that, knowledge being a necessary requirement to render the loan unenforceable, the lender was not put on inquiry whether the money was being borrowed for the purposes of the company's business, notwithstanding that the power to borrow was expressly limited to borrowing for those purposes. That case, therefore, is clear authority for two propositions: (1) that where there is a power to borrow for the purposes of the company's business (even if contained in the objects clause) and the borrowing is made otherwise than for those purposes, the borrowing is not void as being *ultra vires*; and (2) a third party is not put on notice by an express requirement that the power is only exercisable for the purposes of the company's business.

Quite apart from what has been discussed above, even assuming that the third party charges were *ultra vires* the company's memorandum and articles of associationship, they could be saved by s. 20(1) of the Companies Act which reads:

> 20(1) No act or purported act of a company (including the entering into of an agreement by the company and including any act done on behalf of a company by an officer or agent of the company under any purported authority, whether express or implied, of the company) and no conveyance or transfer of property, whether real or personal, to or by a company shall be invalid by reason only of the fact that the company was without capacity or power to do the act or to take the conveyance or transfer.

From the facts as adumberated above, I fail to see how can one contend that the said s. 20(1) has no application. I agree with Counsel for the bank that the said section abolishes the otherwise rigorous effect of the *ultra vires* doctrine. The following passage from the *Sourcebook of Singapore and Malaysian Company Law* by Philip N. Pillai 1975 Edn. at p. 121 cited by the learned Counsel lends support to this proposition:

> Section 20(1) is in my view directly applicable to the plaintiff's contention that a joint borrowing was beyond the power of Landmark Finance. The plaintiff's allegation is that Landmark Finance lacked the power to give this joint debenture to secure joint borrowings. But even if it did, s. 20(1) provides in terms that Landmark Finance's act in that connexion shall not be invalid by reason only of the fact that Landmark Finance was without such power. Generally speaking, subsection (1) strikes down the absolute effect of the *ultra vires* doctrine. An *ultra vires* transaction is no longer a complete nullity, incapable of being recognised as a transaction at all. On the contrary, it is a transaction which, in general terms, is not invalid by reason only of the fact that the company was without the capacity or power to enter in the transaction. But whilst the general nullifying effect of the *ultra vires* doctrine is abolished by s. 20(1), the legislature has marked out certain fields within which significance will still attach to an excess by a company or its officers of the legitimate scope for its activities an enunciated and restricted by the terms of its objects clause.

For the above reasons, I will allow the application of the bank and revoke the order of the Court dated 16 September 1988 granting the stay of the sale of the land by public auction. The plea for leave to set aside the order of the Court directing the sale of the land by public auction made by Metro is also revoked.

Also found at [1991] 1 CLJ 787